Testimony to the

Michigan House Committee on Government Operations

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Thank you for inviting me to testify today. My name is Patrick Wright, and I am the senior legal analyst at the Mackinac Center for Public Policy, a research and educational institute based in Midland.

Public attention to property rights has increased considerably in the past few months because of an important U.S. Supreme Court ruling. On June 23, 2005, the court issued a decision in Kelo v. New London, a case that involved an eminent domain dispute in the state of Connecticut.

The city of New London — described in the Supreme Court's written opinion as a "distressed municipality" — approved a downtown development plan that it believed would create 1,000 jobs and increase its tax revenue. The plan included building a hotel, restaurants, shopping space, office space and a parking lot. Some residents willingly sold their houses to the city, but others, including Susette Kelo, did not.

Ms. Kelo owned a home in the neighborhood targeted for development. She claimed that New London's downtown development plan was not producing a public use; rather, it was merely transferring her property from one private party to another — specifically, from her to a commercial developer.

A 5-4 majority of the Supreme Court disagreed. This decision received a great deal of publicity, and many Americans were surprised to discover that the government could take their homes for a very wide range of reasons, including the purpose of improving its own tax revenue. A silver lining in the otherwise dismal *Kelo* decision was the Supreme Court's proclamation that, "Nothing in our opinion precludes any State from placing further restrictions on its exercise of the takings power." Therefore, this Legislature and the people of this state can limit the situations in which takings can occur.

This committee — and the Legislature as a whole — are correct to review Michigan law and jurisprudence on takings in the wake of the Kelo decision. In the remainder of my testimony today, I will explore the key issues that should be considered in this review and how Michigan's protection of private property rights can be strengthened while preserving the government's power to take property for genuinely public purposes.

A crucial first step is to define what constitutes a taking. When dealing with real property, there are generally two recognized types of takings:

(1) where the government physically occupies or damages a property; and

(2) where the government does not physically invade the property, but where the regulations that impact the property go "too far."

I will talk about the second case, which is commonly referred to as a "regulatory taking," in a few minutes. For the moment, however, let me concentrate on the first case.

In the first case, where there is a physical taking, the taking is supposed to occur only for a "public use." What constitutes this public use was the primary question raised in Kelo, and this question has been answered differently by the United States Supreme Court and the Michigan Supreme Court.

In *Kelo*, the United States Supreme Court held that economic development and the potential for increased tax revenue constitutes a public use. Further, it held that the courts should generally defer to the taking entity's determination of whether the taking was a public use that would genuinely benefit the public.

In her dissent, Justice O'Connor recognized the likely outcome of this ruling. She said:

> Any property may now be taken for the benefit of another private party, but the fallout from this decision will not be random. The beneficiaries are likely to be those citizens with disproportionate influence and power in the political process, including large corporations and development firms. As for the victims, the government now has license to transfer property from those with fewer resources to those with more. The Founders cannot have intended this perverse result.

Fortunately, the U.S. Supreme Court's decision is quite different from the position recently reached by the Michigan Supreme Court. One year ago, in Wayne County v. Hathcock, the state Supreme Court interpreted the term "public use" under the Michigan Constitution, and all seven justices held that so-called economic development of a kind similar to that envisioned in the Kelo case did *not* in fact qualify as a public use.

In Hathcock, the Michigan Supreme Court was reversing one of its most notorious and poorly reasoned decisions — Poletown Neighborhood Council v. Detroit, which was decided in 1981. At the time, five justices of the Michigan Supreme Court ruled that a large neighborhood could be razed in order to make room for an auto assembly plant that Detroit hoped would create jobs and tax revenue in Detroit.

Both the Hathcock Court and the Poletown Court were interpreting Article 10, Section 2, of the Michigan Constitution of 1963, which states the following:

> Private property shall not be taken for public use without just compensation therefore being first made or secured in a manner prescribed by law. Compensation shall be determined in proceedings in a court of record.

Because the state Supreme Court was interpreting the same language in these two different cases but was reaching such different results, some have argued that legislative guidance and even constitutional changes are necessary.

House Bill 5060 would protect private property from being taken for economic development purposes that do not involve the historically common public infrastructure improvements, such as roads, railroads, airports, telephone lines and so forth. The bill would amend MCL 213.23, which is the provision by which public corporations and state agencies are authorized to take property. Under that statute, the taking must be for a public use as defined in the statute (not as defined in the Michigan Constitution, of which the Michigan Supreme Court is the final arbiter). The bill would amend the statute to indicate that a taking is not a public use when the property is transferred to "a private entity for the primary benefit of the private entity."

Respectfully, I would suggest that this additional language, while an improvement, can still leave important property rights vulnerable. Rather than prohibiting a single type of transaction, the Legislature could instead consider affirmatively setting forth the *only* times that a taking *is* proper.

Under a public policy that fully respects America's tradition of property rights, takings should be limited to three instances:

(1) Where the government needs to possess and occupy the land, say for a school, or for a government agency building.

(2) Where necessary to allow instrumentalities of commerce to perform their core functions. For example, an airport authority should have property condemned on its behalf if that property is necessary for an air traffic control tower or a runway. Things like parking and airport shops are not core functions of an airport, and if an airport authority wishes to engage in these activities, then it should acquire the necessary property on the open market, without the use of the coercive power of the state. Other permissible instrumentality-of-commerce functions would include obtaining the land necessary for roads, highways, railroads, ports, sewers, and utilities.

(3) Where necessary to cure blight. Where property is condemned due to blight, the taking entity is generally allowed to transfer that property to another private interest. While blight must be carefully defined, so that it is not applied indiscriminately to, say, all lower-income housing, the provision that blighted property be transferred to a private entity can make sense. The condemned property will usually be a small parcel with a

dilapidated home. By and large, the people who would be interested in small lots would be potential homeowners, not state agencies or schools.

I would note that House Bill 5060 would forbid properties that are condemned for blight from being sold to private parties, such as other homeowners. I am not sure that this was the sponsors' intent.

But I would emphasize again that in addressing blight, care should be taken to ensure that it is determined on a parcel-by-parcel basis, not on neighborhood-by-neighborhood basis. Otherwise, another Poletown-style taking, which wiped out hundreds of viable homes and dozens of businesses, could occur. Homeowners who keep their homes in good shape should not have their property taken merely because a number of their neighbors do not. Further, to protect low-income residents from having their property taken by municipalities that want a higher tax base, blight should be defined to include only improved or unimproved real property that constitutes a danger to the health and safety of the community for the following reasons: contamination, dilapidation (strictly defined), a dangerous lack of water or sanitary facilities, or a combination of these factors.

Of course, in all three of the takings situations I listed a moment ago, just compensation — that is, market value — would have to be paid. The exclusive list of what constitutes a public use would prevent further abuse of the condemnation procedures. It would maximize the protection to the private property holder and make the residents of this state more secure in their homes.

This physical type of taking is not the only one. There is a second type of taking, which I referred to earlier, known as a "regulatory taking."

Regulatory taking was first recognized in Pennsylvania Coal Company v. Mahon, a 1922 decision written by U.S. Supreme Court Justice Oliver Wendell Homes. Justice Holmes recognized that where the diminution of a property's value due to a regulation reached a "certain magnitude, in most if not in all cases there must be an exercise of eminent domain and compensation to sustain the [regulation]." He stated, "The general rule at least is, that while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking."

The question of what constitutes "too far" has proven to be particularly vexing for the courts. For 70 years, the U.S. Supreme Court refused to set a standard for what constituted "too far."

But in 1992, in Lucas v. South Carolina Coastal Council, the Supreme Court set forth one categorical rule. In Lucas, a developer bought two lots that were near, but not on, the South Carolina seashore. When he bought the lots, they were zoned so that he could build single-family homes on them. South Carolina then enacted a law that prohibited any development of any lot that was within a certain distance of the seashore.

Lucas, the developer, was thereby denied any economically valuable use of his land. The Court's touchstone was that if a regulation was passed *after* an owner acquired

an interest in a property that was economically useful, and if the regulation deprived the property of *all* economic utility, then the owner was entitled to just compensation. If, on the other hand, the property were denied only *some* economic use — even if it were as much as 95 percent of its economic use — then the property owner would have to show he or she had suffered a taking under the uncertain ad hoc line of cases that predominated before the Lucas decision.

It is difficult for a property owner to show a taking occurred under the ad hoc test. Take, for example, a farmer who wants to sell a 40-acre parcel of land to create a 40-home subdivision, but finds he is not allowed to develop 10 acres of the property due to wetlands regulations enacted after he obtained it.

Under the ad hoc rules, a key issue would be determining what constitutes the "denominator parcel." After all, the Supreme Court has recognized that where an owner is deprived of *all* use of their land, compensation is required. If the court merely considers the 10 acres where development is prohibited, it would typically determine that a 100 percent taking had occurred and award compensation. If, on the other hand, the court looks at all 40 acres, it could easily conclude that a 25 percent taking had occurred and rule that no compensation is due.

Oddly, then, if the farmer had merely owned 10 acres of wetlands, instead of the entire 40-acre parcel, he would be compensated. Because he owns all 40, however, he may very well get nothing. In both situations, the farmer's monetary loss is the same, but in only one case does society pay for having produced the loss.

The denominator-parcel issue was addressed in the 1995 Michigan Court of Appeals decision Volkema v. DNR. The court held the entire parcel, not just the wetlands portion of it, constituted the denominator parcel. But Judge Sawyer's dissent in that case illustrates the best public policy. He wrote:

> In short, in light of the strong historical protection of private property in this country and the constitutional mandate that the government may put private property to public use only after compensating the owner of that property, I believe that the question . . . is best answered by concluding that a taking occurs where a regulation precludes the use of an identifiable, discreet (sic) piece of property, even if that property forms only a portion of a larger parcel. I do not find it relevant how large a portion of property the owner possesses. What is relevant is that the government has determined that a public purpose would be served by denying the rightful owner of the property the use of that property and requiring it to be used, or in this case not used, in accordance with that public purpose. While the government is permitted to do this, it must compensate the property owner for putting the property to public use. Our historical protection of private property in the constitution allows no less.

Judge Sawyer's method would prevent the arbitrary result that occurs where development on a portion of a parcel is absolutely prohibited, but an economic use remains for another portion of the parcel.

The people of Oregon have recently put this idea into practice with "Measure 37," which was passed on a popular ballot in 2004 with 60 percent of the vote. Measure 37 essentially assumes that the value of a property owners land should be determined only by the marketplace; it should not be diminished by state and local regulations without compensation. If a regulation is enacted in Oregon for the benefit of society, and if that regulation diminishes the value of the land after a property owner has acquired his or her interest in it, society in general must pays the cost. Under Measure 37, the cost is *not* shifted to the landowner.

Thus, if the property were worth $200,000 before the regulation and just $50,000 afterwards, the $150,000 loss is not put entirely on one individual, as it is in most of the country. Rather, it is charged to — and spread throughout — the society that benefits from the regulation.

To prevent financial hardship to the government, Measure 37 allows the regulatory unit of government to modify, negate or not enforce the regulation if it determines that paying the property owner would be too expensive. If the government decides it wants to enforce the regulation, but finds that it is hit for a large award after a trial is held, it can again simply decide not to enforce the regulation on that parcel and forgo paying the award. The property owner would then enjoy use of the property as if the regulation were never passed. Measure 37 also exempted many traditional regulations, such as regulations related to fire safety, health and sanitation, solid or hazardous waste, pollution controls and regulations required by federal law.

In light of the Kelo decision and the regulatory takings concerns that led to the passage of Measure 37 in Oregon, a constitutional amendment would probably be the most secure manner for making ensuring a lasting public policy protection of private property rights. Nevertheless, well-crafted legislation that addresses either of these issues would provide more protection than is currently afforded to the property rights of Michigan citizens.

This is no small consideration. James Madison, who has been called the father of the U.S. Constitution, set forth government's duty concerning property as follows:

> Government is instituted to protect property of every sort. ... This being the end of government, that alone is a *just* government, which *impartially* secures to every man, whatever is his *own*. (Emphasis in original.)

In Federalist No. 51, Madison also discussed the necessity of government accountability:

> If men were angels, no government would be necessary. If angels were to govern men, neither external nor internal controls on government would be necessary. In framing a government which is to be administered by men over men, the great difficulty lies in this: you must first enable the

> government to control the governed; and in the next place oblige it to control itself.

Despite the Michigan Supreme Court's laudable ruling in Wayne County v. Hathcock, further controls are needed to fully protect the people of Michigan from takings abuses like Poletown and Kelo. In that light, I hope you find the comments I provided today useful. Thank you for your time; I would be willing to answer any questions you might have.

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